

Message Text

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ACTION EB-07

INFO OCT-01 AF-06 ARA-06 EUR-12 EA-07 NEA-10 ISO-00 FEA-01

ERDA-05 AID-05 CEA-01 CIAE-00 CIEP-01 COME-00 DODE-00

FPC-01 H-02 INR-07 INT-05 L-03 NSAE-00 NSC-05 OMB-01

PM-04 USIA-06 SAM-01 OES-03 SP-02 SS-15 STR-04

TRSE-00 PA-01 PRS-01 /123 W
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R 191640Z NOV 75

FM AMEMBASSY QUITO

TO SECSTATE WASHDC 8037

INFO AMCONSUL GUAYAQUIL

AMEMBASSY ABU DHABI

AMEMBASSY ALGIERS

AMEMBASSY CARACAS

AMEMBASSY JAKARTA

AMEMBASSY JIDDA

AMEMBASSY KUWAIT

AMEMBASSY LAGOS

AMEMBASSY LIBREVILLE

AMEMBASSY LIMA

AMEMBASSY SANTIAGO

AMEMBASSY TEHRAN

AMEMBASSY TRIPOLI

AMEMBASSY VIENNA

USMISSION OECD PARIS

C O N F I D E N T I A L QUITO 8444

E.O. 11652: GDS

TAGS: ENRG EFIN EINV EC

SUBJECT: ECUADOR RAISES CRUDE PRICE 3.9 PERCENT

1. BEGIN SUMMARY: THE GOE ANNOUNCED NOVEMBER 18 THAT
GOVERNMENT TAKE WOULD BE INCREASED BY 3.9 PERCENT, FROM \$10.17
TO \$10.57 A BARREL. THE GOE FIXED SELLING PRICE FOR ECUADOREAN
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CRUDE FOB BALAO AT \$11.46 A BARREL. REFERENCE PRICE REMAINS

FIXED AT \$13.90 PER BARREL (30 API) AND THE COMPANIES WILL
CONTINUE TO SUPPLY DOMESTIC COMSUMPTION AT \$1.48 A BARREL.
END SUMMARY.

2. AFTER THE GOE'S PROLONGED AND APPARENTLY HEATED
CONSIDERATION OF POSSIBLE PRICE INCREASES, MINISTER OF
NATURAL RESOURCES JAIME DUENAS ANNOUNCED NOVEMBER 18
A 3.9 PERCENT INCREASE IN GOVERNMENT TAKE. ACCORDING TO
PETROLEUM INTELLIGENCE WEEKLY, THE PERCENTAGE INCREASE IS
THE LOWEST OF ALL OPEC COUNTRIES WITH THE EXCEPTION OF
INDONESIA. THE MINISTER JUSTIFIED THE SMALL INCREASE BY
SAYING THAT EACH OPEC MEMBER IS ALLOWED TO ESTABLISH ITS
PRICE BASED ON ITS PARTICULAR MARKET CONDITIONS: I.E.,
ECUADOR'S RELATIVE LOSS OF ADVANTAGE FOR ITS LOW SULFUR CONTENT,
THE PANAMA CANAL TRANSPORT CHARGE AND A 9-CENT DISCOUNT
FOR CREDIT TERMS OFFERED BY SOME OTHER PRODUCERS. DUENAS
EMPHASIZED, HOWEVER, THAT THE PRICE COULD BE REVISED IN
DECEMBER IN ACCORDANCE WITH "MARKET FACTORS".

3. THE GOE FIXED "MARKET" PRICE OF ECUADOREAN CRUDE AT
(11.46 PER BARREL. TEXACO-GULF OFFICIALS HAVE TOLD EMBASSY
OFFICERS THAT THEY SUPPLIED THE MINISTRY WITH VARIOUS MARKET
PRICES FOR ECUADOREAN CRUDE RANGING FROM \$11.26 TO \$11.64.
THE MINISTRY SIMPLY AVERAGED THE COMPANY CALCULATIONS TO
ARRIVE AT ITS DECREED SALES PRICE FOR ECUADOREAN CRUDE.
IN PREVIOUS PRICE CHANGES, THE MINISTRY OF NATURAL RESOURCES
HAS NEVER PUBLICLY ESTABLISHED SALES PRICE SINCE SALES ARE
ESSENTIALLY INTERNAL COMPANY TRANSACTIONS. IN HEADLINE
COVERAGE, THREE OF THE FOUR MAJOR NEWSPAPERS REPORTED
THAT THE PRICE OF ECUADOREAN CRUDE HAD INCREASED FROM
\$10.41 TO \$11.46 A BARREL, AN EXACT INCREASE OF 10
PERCENT. POSSIBLY THE MINISTRY ITSELF PROMOTED THIS
MISUNDERSTANDING TO DEFLECT PUBLIC CRITICISM, ALTHOUGH
ACTUAL MINISTRY REGULATIONS ISSUED NOVEMBER 18 ARE QUITE
CLEAR ABOUT AN INCREASE OF ONLY 3.9 PERCENT. THE PRESS
COVERAGE, HOWEVER, DOES OBFUSCATE THE VERY MODERATE PRICE
INCREASE.

4. UNDER THE NEW SYSTEM THEORETICAL CONSORTIUM PROFIT IS
APPROXIMATELY 44 CENTS A BARREL. THE COMPANIES HAVE BEEN
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GIVEN CREDIT FOR APPROXIMATELY 20 CENTS PER BARREL OF THE
NORSAL-PHOENIX PAYMENT (WHICH WAS ESSENTIALLY IGNORED IN
PAST GOE CALCULATIONS), AND THE COMPANIES NOW CLAIM THEIR
THEORETICAL PROFIT IS ONLY A FEW CENTS LESS THAN GOE
ESTIMATES:

FOB BALAO	\$11.46	
PREVIOUS GOE TAX-PAID COST		\$10.41
	\$ 1.05	

NORSAL-PHOENIX PAYMENT	\$.21
	\$.84

INCREASE IN GOVERNMENT TAKE	\$.40
COMPANY MARGIN	\$.44

5. THE GOE ALSO REVISED, BUT DID NOT ACTUALLY SIMPLIFY, ITS COMPLICATED TAX STRUCTURE, THE INCREASE IN GOVERNMENT TAKE OF 40 CENTS PER BARREL WAS ACCOMPLISHED BY RAISING ROYALTIES FROM 16.67 PERCENT TO 17 PERCENT. NUMEROUS GOE TAXES WERE CONSOLIDATED INTO A NEW "UNIFIED TAX" OF 71.42 PERCENT. OTHER MINOR TAXES OF APPROXIMATELY 17 CENTS PER BARREL WERE NOT INCLUDED IN THE NEW REGULATIONS. DISTRIBUTION OF PETROLEUM REVENUES REMAINS APPROXIMATELY THE SAME UNDER THE NEW SYSTEM ALTHOUGH THE ECUADOREAN STATE PETROLEUM COMPANY (CEPE) WILL RECEIVE 20 CENTS PER BARREL OF THE 40 CENTS INCREASE IN GOVERNMENT TAKE.

6. THE CURIOUS POINT IS WHY ECUADOR RAISED GOVERNMENT TAKE BY AS MUCH AS 40 CENTS, ALBEIT A VERY MODERATE PRICE INCREASE RELATIVE TO OTHER OPEC MEMBERS. A WIDELY DISSEMINATED MINISTRY PROPOSAL (KNOWN TO HAVE THE FULL SUPPORT OF MINISTER OF NATURAL RESOURCES JAIME DUENAS) SUGGESTED AN INCREASE IN STATE PARTICIPATION OF APPROXIMATELY 33 CENTS A BARREL AND THUS AN INCREASE IN COMPANY MARGINS TO SOME 50 CENTS A BARREL. OFFICIALS OF TEXACO-GULF ESSENTIALLY EXPECTED DUENAS' PROPOSAL TO BE IMPLEMENTED AND FREQUENTLY LOBBIED WITH MINISTRY OF NATURAL RESOURCES OFFICIALS FOR A SMALL INCREASE IN GOVERNMENT TAKE. APPARENTLY CEPE OFFICIALS (NOTABLY CEPE MANAGER COL. RENE VARGAS) AS WELL AS OTHER GOVERNMENT OFFICIALS CLAIMED THE INCREASE WAS INADEQUATE TO PROMOTE CEPE'S AMBITIOUS PLANS FOR EXPLORATION

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AND DEVELOPMENT. RESIGNATION OF THE MINISTRY COMMITTEE CHARIMAN, JORGE PAREJA, PUBLICLY CRITICIZED FOR CONFLICT OF INTEREST BECAUSE OF PREVIOUS EMPLOYMENT IN GULF'S FINANCIAL DEPARTMENT, DAMAGED THE MINISTRY PROPOSAL. HOPEFULLY DUENAS WILL BE ABLE TO CONSOLIDATE HIS POWER BASE AND INCORPORATE CEPE FULLY UNDER HIS CONTROL WITH VARGAS' RESIGNATION, WHICH IS EXPECTED IN THE NEXT FEW MONTHS.

7. PERHAPS, HOWEVER, CEPE'S INCREASE OF THE 20 CENTS PER BARREL IN GOVERNMENT TAKE WILL OFFER INDIRECT ADVANTAGES TO THE TEXACO-GULF CONSORTIUM. CEPE PRESENTLY OWES TEXACO-GULF SOME \$20 MILLION FOR ITS 25 PERCENT SHARE OF OPERATING COSTS (THE COMPANIES ADD THIS THEORETICAL INTEREST CHARGE TO THEIR TAX-PAID COST). CEPE ALSO HAD REJECTED ITS 25 PERCENT SHARE OF THE \$165 MILLION INVESTMENT PLAN BECAUSE

OF CHRONIC LACK OF FUNDS. TEXACO-GULF IS NOT ONLY RELUCTANT TO IMPLEMENT THE INVESTMENT PLAN BECAUSE OF INADEQUATE PRICE INCENTIVES, BUT ALSO BECAUSE CEPE HAD REFUSED TO ASSUME ANY NEW INVESTMENT OBLIGATIONS. IT REMAINS TO BE SEEN WHETHER CEPE, ALREADY IN A HIGHLY ADVANTAGEOUS TAX POSITION VIS-A-VIS TEXACO-GULF, WILL BE CAPABLE OF MAKING SIGNIFICANT INVESTMENTS. BUT CEPE'S INCREASED REVENUES OF SOME \$800,000 PER MONTH SHOULD FACILITATE REIMBURSEMENT OF OPERATING COSTS.

8. COMPANY REACTION TO THE PRICE INCREASE HAS BEEN GUARDED. BOTH TEXACO AND GULF OFFICIALS HAD TOLD EMBASSY OFFICERS THAT THE THEORETICAL PROFIT OF 50 CENTS WOULD NOT BE SUFFICIENT TO IMPLEMENT THE ENTIRE \$165 MILLION INVESTMENT PLAN, BUT HINTED THAT SOME OF THE INVESTMENT COULD BE MADE AT THIS PROFIT LEVEL. TEXACO AND GULF WERE CAREFUL TO SAY, HOWEVER, THAT LONG-RANGE PROFITABILITY IS DEPENDENT ON WORLD MARKET CONDITIONS AND POSSIBLE OTHER INVESTMENT INCENTIVES THAT MAY BE OFFERED BY THE GOE. THE COMPANY REACTION, AT LEAST A PARTIAL INDICATION THAT SOME OF THE INVESTMENT PLAN COULD BE IMPLEMENTED, IS A DRASTIC CHANGE FROM PRIOR COMPANY COMPLAINTS THAT MAINTENANCE OF EQUIPMENT WAS NOT ECONOMICALLY JUSTIFIABLE. COMPANY OFFICIALS HAVE TOLD EMBASSY OFFICERS THAT THE CONSORTIUM LOST MILLIONS OF DOLLARS THIS YEAR. NOW COMPANY OFFICIALS ESTIMATE A PROFITABILITY LEVEL AT THE NEW PRICE OF SOMEWHERE AROUND 13 PERCENT--PERHAPS NOT ENOUGH TO WARRANT MUCH INVESTMENT, CONFIDENTIAL

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BUT IT IS CERTAINLY NOT THE RED INK SITUATION THAT PREVAILED A FEW MONTHS AGO.

9. NO DECREE HAS YET BEEN PROMULGATED, BUT TRANSLATION OF GOVERNMENT REGULATIONS ISSUED NOVEMBER 18 WILL FOLLOW BY POUCH.
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